SUPREME JUDICIAL COURT

Boston, Massachusetts 02108

NOTICE OF APPROVAL

Notice is hereby given that the Supreme Judicial Court has approved and promulgated rules as further indicated below.

MARGARET H. MARSHALL
Chief Justice

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1. Court Submitting Rules for Approval:

   IOLTA Committee

2. Date Rules Submitted for Approval:

   June 30, 2006

3. Date Approved and Promulgated by the Supreme Judicial Court:

   July 26, 2006

4. Rules or Rules, or Amendments Thereto, Approved and Promulgated:

   Amendments to IOLTA Guidelines

   Effective date - The IOLTA Committee is authorized to implement the revised Guidelines on or before January 1, 2007.

(The original of this notice is to be filed in the office of the Clerk of the Supreme Judicial Court for the Commonwealth, and a copy to be sent by the Clerk to the court which requested approval of the rules.)

**MASSACHUSETTS IOLTA COMMITTEE**
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June 30, 2006

Honorable John M. Greaney
Chair
SJC Rules Committee
John Adams Courthouse
One Pemberton Square
Boston, MA 02108

RE: Proposed IOLTA Guideline Changes

Dear Justice Greaney:

I write on behalf of the Massachusetts IOLTA Committee to request two revisions to the Interest on Lawyers Trust Accounts Committee Guidelines (Guidelines), which were last revised by the Court in November 1993. The IOLTA Committee collects interest on lawyers trust accounts that would not otherwise generate interest for clients. It passes these revenues along to three charitable entities that make grants to assist the administration of justice and support legal aid to the poor.

The first proposed revision concerns the interest rates paid by financial institutions on IOLTA accounts. The second is intended to conform the Guidelines to the 2004 amendments to Mass. R. Prof. C. 1.15 Record Keeping Rules. The text of the proposed revisions begins on page 8 of this letter, as Attachment 1.

These revisions were initially proposed to the Rules Committee by the IOLTA Committee on March 9, 2006. At that time it was suggested by the SJC that the proposed revisions be published for public comment. The IOLTA Committee had the proposed revisions published for comment in Massachusetts Lawyers Weekly on March 13, 2006. In addition, letters requesting comments were sent to each of the 200 financial institutions that offer IOLTA accounts. Enclosed as Attachment 2 is a copy of the letter and enclosure. Comments were due no later than April 28, 2006. Nine comments were received, all relating to the interest rates revision. The Massachusetts Bankers Association also requested a meeting to discuss the proposed revisions; that meeting was held on May 24, 2006.

The Committee carefully reviewed these comments and considered changes in the proposed revisions. The comments are discussed in Part III of this letter. The Committee, in response to the comments, has amended its proposed revision to the interest rate guideline. The Committee now proposes that the Court approve the Guideline revisions, as amended, set forth beginning on page 8.

## I. Fair and Reasonable Interest Rates

Fair and reasonable interest rates on IOLTA accounts generate appropriate levels of revenue to provide legal services to low income citizens in Massachusetts while not placing financial institutions at an economic disadvantage. In recognition of the crucial role played by interest rates in the generation of IOLTA revenue, the Supreme Judicial Court (SJC) in 1993 approved an amendment to the Guidelines that called for financial institutions to pay interest "at a rate equal to or greater than the financial institution pays on NOW or comparable interest bearing accounts."

When this wording was adopted, NOW account rates were between 4 and 5%. In 2004, IOLTA account rates throughout the country ranged from 0.35% to 1.2%, with a weighted national average for all accounts of approximately 0.51%. This slippage was caused by the competitive evolution in bank deposit products since the early 1980s. Interest-bearing checking accounts were a new bank deposit product when IOLTA came into being, but they are now a commodity commanding an interest rate near the bottom for any types of accounts offered by banks. By pinning IOLTA interest rates to NOW accounts, the current Guidelines cause IOLTA revenue to fluctuate based on this product rather than on the complete competitive market for earnings on deposits.

Competition for deposits has encouraged banks to develop new products, such as business sweep accounts, that can bring in and retain customers whose business requires them to keep large average balances on deposit. Interest rates for those accounts move up and down in tandem with various indices such as the Federal Funds Rate. Rates for interest-bearing checking accounts, on the other hand, are relatively insensitive to increases in these indices. IOLTA accounts - even large ones - remain in this relatively low-priced NOW configuration because neither banks nor law firms have had incentives to change the status quo.

We are requesting that the Guidelines be updated so that IOLTA accounts earn the same interest generally available to similarly situated non-IOLTA customers at the same financial institution. This would continue the intention of the 1993 Guidelines, and reflect the current market for financial products. The new language is also more flexible than that of the current Guidelines, and will permit natural adjustments as financial products evolve in the future, assuring that financial institutions treat IOLTA accounts fairly.

The Federal Reserve Bank has increased the Federal Funds Rate 17 times during the past twenty-four months; the rate is now at 5.25%. Despite these increases, most smaller banks in Massachusetts are still offering interest rates on IOLTA accounts that are less than one-half of one percent (.005). The rates paid by the larger banks are generally better, but are still a third or less of the Federal Funds rate, generally about 1.50%. This is not a new pattern. Enclosed as Attachment 3 is a chart showing how bank IOLTA rates fall when the Federal Reserve lowers interest rates and fail to increase when the

Federal Reserve rates increase. IOLTA rates have stayed well below the Federal Reserve rates, and well below the lowest deposit account rates.

Several states have amended their IOLTA rules to ensure uniform and fair treatment of IOLTA rates by their banks. States which have implemented language similar to that proposed here for our Guidelines are Alabama, Connecticut, Florida, Indiana, Michigan, New Jersey, Ohio, Pennsylvania, and Utah. Their new provisions require that financial institutions pay rates on IOLTA accounts which are comparable to the rates paid on other products with balances similar to IOLTA accounts. Enclosed as Attachment 4 is a chart with the language of several states' comparable rate guidelines.

The Massachusetts IOLTA Committee has studied the materials from these states and noted that in November of 2005 the New Jersey Supreme Court adopted a "Best Customer Standard" (described within Attachment 4). The Court stated, "(t)his standard describes the actions necessary to demonstrate that a financial institution is offering a comparable and reasonable return on IOLTA accounts, as required by the IOLTA Guidelines."

In order to maximize the return on IOLTA investments, for the benefit of the charities, the Massachusetts IOLTA Committee believes banks should be fair and provide parity between the interest rates they pay on IOLTA accounts and the interest rates they pay on otherwise comparable non-IOLTA accounts. On January 12, 2006, the IOLTA Committee voted to request that the Supreme Judicial Court approve the proposed Guideline. The proposed Guideline updates rate parity requirements to provide that IOLTA accounts receive the highest interest generally available to an institution's own non-IOLTA customers as long as the IOLTA accounts meet the same minimum balance and other account eligibility requirements as the non-IOLTA customers.

The changes in the proposed Guideline bring the IOLTA framework into alignment with 21st century banking practices and investment options which are now available. The rate parity provisions only affect banks which already offer higher rate products to non-IOLTA customers for similar balances. These provisions are inherently fair to banks because they rely on a bank's own existing products, which are already structured to be profitable to the bank.

IOLTA always has been and remains voluntary for banks. Banks do not have to offer IOLTA accounts. Lawyers, however, are bound by the IOLTA Rules and may only place their trust funds at institutions that meet the Rules' requirements. To assist with implementation, the Committee will work with each affected bank and with affected lawyers as needed.

II. Change in the Record Keeping Rules

To conform to the revised ethical rules, we are requesting minor changes in the Guidelines which recognize that all references to Mass. R. Prof. C., 1.15 (e) need to be changed to Mass. R. Prof. C., 1.15 (g) .

III. Comments to the Proposed Revisions

The proposed revisions were published for public comment in Massachusetts Lawyers Weekly on March 13, 2006. Comments were due no later than April 28, 2006. The first proposed revision of the Guidelines was to modify the description of interest rate options available to financial institutions that offer IOLTA accounts to attorneys. The Committee received nine comments to this proposal: six from banks, one from a banking trade association and two from charitable entities that receive IOLTA funds and make grants to providers of free legal services to the poor and for improvements in the administration of justice. The second proposed revision of the Guidelines was for the purpose of conforming the Guidelines to the 2004 Record Keeping amendments in Mass. R. Prof. C., Rule 1:15. No comments were received regarding this revision.

With regard to the description of interest rate options available to financial institutions that offer IOLTA accounts to attorneys, the IOLTA Committee reviewed these comments carefully as detailed in the following section by section analysis:

Section by Section Analysis of Comments:

The proposed revision substitutes a requirement that a financial institution pay interest at a rate "comparable to the highest rate of return the financial institution offers according to" a new "Best Customer Standard" for the current rule's requirement that the interest rate be "equal to or greater than the financial institution pays on NOW accounts or comparable interest bearing accounts."

The two charitable entities that commented, the Massachusetts Bar Foundation and the Massachusetts Legal Assistance Corporation, gave full support to the proposed revision because it would appropriately increase the financial support available to critical legal assistance programs that serve some of the Commonwealth's most vulnerable residents. They noted that the "Best Customer Standard" would remedy inequities in the rates banks pay across the state.

The "Best Customer Standard" is defined in two alternative subsections. Under Section B.1.A., a financial institution can meet the "Best Customer Standard" by providing to IOLTA "the highest yield available among" four types of accounts, "as provided to the best customers of the institution with similarly-sized deposits in such accounts in Massachusetts." The four types of accounts are:

1. a money market with or tied to check writing capability;
2. a business checking account with an automated investment feature, such as an overnight sweep or other automated transfer, and investment in insured bank accounts, or repurchase agreements fully collateralized by U.S. government securities;
3. a government (such as municipal deposits) checking account; [or]
4. any other interest-paying business checking account product.

Many of the bank comments, and the comment of the trade association, misunderstood this subsection. These comments pointed out that the four types of accounts often are offered subject to terms and conditions such as maximum activity levels, minimum balance requirements, monthly fees and other limitations. The Massachusetts Bankers Association comment misstated the standard as requiring a rate "at least equal to the rate paid to the best customers of that specific institution with similarly sized balances, regardless of transaction activity, loan balances or other accounts."

In fact, the "Best Customer Standard" only called for rates paid under the same terms and conditions "as provided to the best customers." Unless a bank chooses to avail itself of the option offered in Section B.1.A.5., it would apply all the same terms and conditions on IOLTA accounts as on the comparable accounts. IOLTA deposits, in order to earn a higher rate of interest, would be subject to the same activity levels, balance requirements and monthly fees. It is true that IOLTA accounts cannot be "linked" to other accounts for minimum balance purposes. This means that an IOLTA account would have to meet all account requirements without benefit of linkage; if it doesn't, then the IOLTA account would not qualify for the rate of interest paid by that type of account.

A similar misunderstanding appeared in one comment noting that sweep accounts are not insured by FDIC. Although the current rules require FDIC coverage, there is an exception for IOLTA accounts in excess of $100,000 reinvested in repurchase agreements fully collateralized by U.S. Government obligations. See Mass.R.Prof.C. 1.15 (g).

One comment correctly noted that many banks currently absorb normal expenses by waiving normal service charges and administrative costs on IOLTA accounts. Such charitable support for IOLTA accounts is not required by the IOLTA Guidelines, although it is certainly encouraged by the IOLTA Committee. As banks do for check printing, they can bill the attorney for the expenses related to the account. A bank meeting the "Best Customer Standard" would not be required to absorb such expenses unless it also absorbed them for its best customers.

Despite the fact that none of the comments identified an actual problem with the proposed definition of "Best Customer Standard" under subsection B.1.A., the Committee realized that the proposed language on the "Best Customer Standard" was not sufficiently clear. At the meeting with the Massachusetts Bankers Association, the Committee invited the Massachusetts Bankers to suggest language that would remove the confusion. The Massachusetts Bankers Association proposed the so-called Connecticut Rule, from the IOLTA Rule recently adopted by Connecticut.

The Connecticut standard (as well as the Michigan, Pennsylvania, Florida and Alabama Rule) is a comparability rule which calls for the financial institution to pay interest comparable to the highest rate of return the financial institution offers to its non- IOLTA account customers when the IOLTA account meets or exceeds the same minimum balance and other account eligibility qualifications applicable to those other accounts.

The Committee agrees with this suggestion and has substituted Connecticut's "comparability" interest standard for the "Best Customer Standard" in the proposed revision. Descriptions of comparable rates and comparability options have been added which make it clear that the IOLTA rate takes into account the eligibility qualifications.

The Committee's proposed revision continues to offer financial institutions a "safe harbor" as an alternative to certifying the highest yield available among comparable accounts. A definition has been added for clarity. The Committee's original proposal placed the safe harbor at 60% net yield of the Fed Funds Target Rate, which followed most states examples. The Massachusetts Bankers Association proposed 50% net yield of the Fed Funds Target Rate following its meeting with the Committee. The proposal was based on banks practice of waiving normal service fees on IOLTA accounts. The Committee considered the proposal but decided that 55% net yield was a fair and reasonable given what banks earn on comparable commercial accounts. The Committee noted that the 60% net yield rate in New Jersey was recently accepted by Bank of America and Sovereign Bank, which were two of the banks that submitted written comments and are two of the largest depositories of IOLTA accounts in Massachusetts.

Conclusion

The IOLTA Committee, having reviewed all the comments received and having adopted changes in the proposed revisions that respond to the comments of the Massachusetts Bankers Association, hereby submits the attached proposals for revision of the IOLTA Guidelines to the Supreme Judicial Court for approval. If approved by the Court, the Committee requests a September 1, 2006 effective date in order to start the lengthy implementation process.

Thank you for the opportunity to submit this request. Please do not hesitate to call if you need further information. We look forward to the Court's response.

Very truly yours,

Anthony M. Doniger,
Chair

cc:
Honorable Judith A. Cowin
Honorable Roderick L. Ireland
Christine Burak
Francis Ford
Richard Soden
Janet Kenton-Walker
Georgia Katsoulomitis
Beth Lynch
Lonnie Powers
IOLTA Committee
Stephen Casey
Jayne Tyrrell

Revisions to the
Interest on Lawyers Trust Account Committee Guidelines:

I. To Assure Fair and Reasonable Interest Rates:

Replace:
B. Characteristics of Accounts
Lawyers shall establish and maintain IOLTA accounts which have the following characteristics:

1. Interest Rates: The financial institution pays interest at a rate equal to or greater than the financial institution pays on NOW accounts or comparable interest bearing accounts.

With:
B. Characteristics of Accounts
Lawyers shall establish and maintain IOLTA accounts in eligible financial institutions which have the following characteristics:

1. Interest Rates: The financial institution pays interest comparable to the highest yield the financial institution offers to its non-IOLTA customers when the IOLTA account meets or exceeds the same minimum balance and other eligibility requirements.

(a) Comparability Options.

A financial institution shall pay on IOLTA accounts the highest yield available among the following product option types (if the product option is available from the financial institution to other non-IOLTA customers) by either using the identified account option as an IOLTA account or paying the equivalent yield on the existing IOLTA account in lieu of actually using the highest yield bank product:

1. A business checking account with an automated investment feature, such as an overnight sweep and investment in repurchase agreements fully collateralized by U.S. government securities as described in Mass.R.Prof.C. 1.15 (g) (1).

2. A government (such as for municipal deposits) interest bearing checking account.

3. A checking account paying preferred interest rates, such as money market or indexed rates.

4. An interest bearing checking account such as a negotiable order of withdrawal (NOW) account, or business checking account with interest.

5. Any other suitable interest bearing deposit account offered by the institution to its non-

IOLTA customers.

As an alternative, the financial institution may pay:

6. A "safe harbor" equal to 55% net yield of the Federal Funds Target Rate. *

7. A yield specified by the IOLTA Committee, if the Committee so chooses, which is agreed to by the financial institution. Such yield would be in effect for and remain unchanged during a period of no more than twelve months from the inception of the agreement between the financial institution and IOLTA.

(b) Implementation of Comparability.

The following considerations will apply to determinations of comparability:

Accounts which have limited check writing capability required by law or government regulation may not be considered as comparable to IOLTA in Massachusetts. This, however, is distinguished from checking accounts which pay money market interest rates on account balances without the check writing limitations. Such accounts are included in the Option 3 class identified above. Additionally, rates that are not generally available to other account holders, such as special promotional rates used to attract new customers, are not considered for comparability in Massachusetts.

For the purpose of determining compliance with the above provisions, all participating financial institutions shall report in a form and manner prescribed by the IOLTA Committee the highest yield for each of the accounts they offer within the above listed account types. The IOLTA Committee will certify participating financial institutions compliance with these Guidelines on an annual basis.

*The IOLTA Committee will review and may revise the safe harbor rate from time to time based on changing market conditions.

(c) Definitions.

An "eligible financial institution" for IOLTA accounts is a financial institution that meets the requirements of Mass. R. Prof. C. 1.15 (g) (1), and has been certified by the Committee to be in compliance with these guidelines.

A "safe harbor" rate, as identified by the IOLTA Committee, is a rate which if paid by the financial institution on IOLTA accounts shall be deemed as a comparable return, regardless of the highest yield available at the financial institution. Such yield shall be calculated based on 55% net yield of the Federal Funds Target Rate as reported in the Wall Street Journal on the first business day of the calendar month.

"Net yield" is defined as the effective interest rate earned on the IOLTA account after considering any fees assessed by the financial institution against the interest earned. Allowable fees are defined at IOLTA Guidelines, B (3) (a) and (b).

II. To Conform to the Revised Record Keeping Rules:

In the Preamble:

1. Replace: The IOLTA Committee ("Committee") provided for by Mass.R.Prof.C. 1.15 (e)(4)(v)(Rule 3:07), adopts the following Guidelines, subject to the approval of the Court, to provide the operation of the comprehensive IOLTA program set forth in amendments to SJC Rule 3:07 adopted by Orders of the Court dated September 26, 1989, October 1, 1992, and April 6, 1993.

With:
The IOLTA Committee ("Committee") provided for by Mass.R.Prof.C. 1.15 (g)(4)(v)(Rule 3:07), adopts the following Guidelines, subject to the approval of the Court, to provide the operation of the comprehensive IOLTA program set forth in amendments to SJC Rule 3:07 adopted by Orders of the Court dated September 26, 1989, October 1, 1992, and April 6, 1993.

2. Replace:
3.(b) Expenses of Charities: ... (b) Compliance...preparing the reports required by Mass.R.Prof.C. 1.15 (e)(6)(Rule 3:07), or...

With:
3.(b) Expenses of Charities: ... (b) Compliance...preparing the reports required by Mass.R.Prof.C. 1.15 (g)(6)(Rule 3:07), or....

3. Replace:

4. Record Keeping:.... (a) have ...annual report required by Mass.R.Prof.C. 1.15 (e)(6)(Rule 3:07); and,....

With:
4. Record Keeping:.... (a) have ...annual report required by Mass.R.Prof.C. 1.15 (g)(6)(Rule 3:07); and,....

4. Replace:
F. Annual Reports
The Committee... required of the charities by Mass.R.Prof.C.1.15 (e)(6)(Rule 3:07)....

With:
F. Annual Reports
The Committee... required of the charities by Mass.R.Prof.C.1.15 (g)(6)(Rule 3:07)....